IN THE
SUPREME COURT
STATE OF MISSOURI

DYNO NOBEL, INC.,

APPELLANT,

v.

DIRECTOR OF REVENUE, STATE OF MISSOURI,

RESPONDENT.

FROM THE MISSOURI ADMINISTRATIVE HEARING COMMISSION
THE HONORABLE WILLARD C. REINE, COMMISSIONER

BRIEF OF APPELLANT

BRYAN CAVE LLP
Edward F. Downey, #28866
221 Bolivar Street, Suite 101
Jefferson City, Missouri 65101
Telephone: (314) 556-6622
Facsimile: (314) 556-6630

Juan D. Keller, #19864
B. Derek Rose, #44447
One Metropolitan Square
211 North Broadway, Suite 3600
St. Louis, Missouri 63102-2750
Telephone: (314) 259-2000
Facsimile: (314) 259-2020
Attorneys for Appellants

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JURISDICTIONAL STATEMENT

This case involves a claim for refund of Missouri use tax Appellant remitted to the Director of Revenue in connection with a unique transaction involving the sharing of costs to operate an on-site utilities plant serving a manufacturing facility owned and operated by two unrelated corporations. Specifically, the primary issue in this case is whether the Appellant's payments to Hercules, Inc., the other corporation occupying the manufacturing plant, to reimburse Hercules for its costs to operate the electricity generation aspect of an on-site utilities plant under a unique Cost Sharing Agreement constituted the taxable purchase of electricity within the meaning of Sections 144.020.1(3) and 144.010.1(9).[1] A secondary issue is whether, assuming, *arguendo*, that the reimbursements constituted purchases of electricity within the meaning of Sections 144.020.1(3) and 144.010.1(9), Appellant was legally obligated to remit Missouri sales tax to the Director under Section 144.060 on those reimbursements since those transactions occurred entirely within Missouri and Appellant provided no written claim of exemption to Hercules.

The Administrative Hearing Commission determined: (a) that Appellant's reimbursements under the Cost Sharing Agreement constituted taxable purchases of electricity within the meaning of Sections 144.020.1(3) and 144.010.1(9); and (b) that Appellant, as the Missouri "purchaser" of electricity from a Missouri "seller," was legally obligated to remit tax to the Director even though Appellant never made any written claim of exemption.

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[1] All statutory citations are to the Revised Statutes of Missouri of 2000, as amended, unless otherwise noted.

Thus, the Court's review of this case will necessarily involve the construction of Sections 144.020.1(3), 144.010.1(9) and 144.060, all of which are revenue laws of the State of Missouri. This Court has exclusive jurisdiction over these issues pursuant to Article V, § 3 of the Missouri Constitution.

STATEMENT OF FACTS

Introduction

This appeal arises out of a unique business relationship between Appellant Dyno Nobel, Inc. ("Dyno") and Hercules, Inc. ("Hercules"). During the periods October 1994 through September 1997 ("Tax Periods"), Dyno and Hercules shared a manufacturing plant near Louisiana, Missouri ("Facility") that produced various chemicals, including ammonium nitrate. The Facility was designed for one occupant and was served by an on-site utilities plant ("Utilities Plant") that provided the Facility's needs for water, steam, and electricity. When Dyno purchased part of the Facility from Hercules in 1985, Hercules and Dyno entered into an agreement for apportioning the cost of operation of the Utilities Plant, the ownership of which was retained by Hercules ("Utility Agreement"). The primary issue is whether Dyno's payments to Hercules for the costs of operating the Utilities Plant to produce electricity constitute taxable purchases of electricity within the meaning of Sections 144.020.1(3) and 144.010.1(9). A secondary issue is whether, assuming, *arguendo*, that the cost reimbursements constitute the taxable purchase of electricity, Dyno is legally obligated to remit Missouri tax notwithstanding that the reimbursement transactions occur entirely within Missouri and Dyno never provided any written claim of exemption.

The fundamental facts are not in dispute and the parties presented the case to the Commission on cross-motions for summary determination. In sustaining the Director's motion, the Commission determined that the cost reimbursements under the Cost Sharing Agreement constituted the taxable purchase of electricity, principally relying on words in the Cost Sharing Agreement between Dyno and Hercules (L.F. 172-73). The Commission further concluded that even though sales tax was due from

Hercules on the transactions rather than use tax from Dyno, Dyno was nonetheless entitled to no refund of use tax (L.F. 175).

Parties and the Facility

Dyno is a Delaware corporation doing business and in good standing in Missouri (L.F. 159). Prior to May 29, 1985, Hercules owned the entire Facility. On that date, Dyno[2] acquired from Hercules, under an Asset Purchase Agreement, all parts of the real property, improvements and equipment used to produce ammonium nitrate (L.F. 159). Dyno's and Hercules' respective portions of the Facility are separated by a cyclone fence (L.F. 159). Since 1985, Dyno has manufactured chemicals, including ammonium nitrate at its part of the Facility (L.F. 159). Hercules has always owned and operated the other part of the Facility to manufacture chemicals (L.F. 159).

The Facility was designed to be occupied and operated by one entity (L.F. 159). The Facility contains the on-site Utilities Plant that produces water, steam and electric power for use in the Facility (L.F. 159). Hercules has always owned the Utilities Plant (L.F. 159). The Utilities Plant operates in the following manner: Hercules draws water from the Mississippi River, treats it and pumps it to Dyno's part of the Facility (L.F. 160). Dyno heats the water and pumps it back to Hercules' portion of the Facility for use in boilers that produce steam that is used at the Utilities Plant to drive steam turbines and generators that produce the electricity that Hercules and Dyno use at the Facility (L.F. 160). In addition to driving the turbines and generators, Dyno and Hercules use steam throughout the Facility for their production operations (L.F. 160).

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[2] Dyno's name was changed from IRECO, Inc. to Dyno Nobel, Inc. in 1985 (L.F. 67, 150).

The Utilities Plant employs two 7.5 megawatt generators to produce electricity for the Facility (L.F. 159). If demand for electricity at the Facility exceeds the output of the two generators, supplemental power is purchased from Union Electric Company ("Union Electric") or Ameren UE, Inc. ("Ameren") (L.F. 88-89, 93-94, 100-01). If the output of the two generators exceeds the Facility's demand for power, Union Electric or Ameren purchase the excess power (L.F. 88-89, 93-94, 100-01). Hercules, as the operator of the Utilities Plant, initially pays sales or use tax on purchases of fuels, the net purchases of supplemental electricity, and other taxable purchases for the Utilities Plant (L.F. 88-89, 93-94, 100-01), but, as for other purchases, Dyno reimburses Hercules for its share of these taxes. Dyno and Hercules also share other costs. For instance, they share the cost of operating and maintaining the Facility's common store-room and the Highway 79 crossing signal (L.F. 168).

Utility Agreement

Section 5.16 of the Asset Purchase Agreement, provided that Hercules and Dyno "shall … agree in writing upon the provisions of common services … including … appropriate sharing of raw materials and utilities" (L.F. 160). Pursuant to a written Utility Agreement drafted pursuant to the Asset Purchase Agreement, Dyno is required to pay two components of the cost of operating the Utilities Plant in connection with its production of electricity for the Facility (L.F. 89, 94, 100-01). Part III, section XI of the Utility Agreement requires Dyno to reimburse Hercules for forty-five percent of the fixed costs of the Utilities Plant, including the cost of labor, overhead, depreciation, property taxes and other fixed costs regardless of whether Dyno uses any electricity at the Facility (L.F. 65-66, 88-89, 93-94, 100-01).

On a number of occasions in the 1990's, the Facility was shut down for extended periods of time (L.F. 167). First, Dyno shut down its manufacturing operations for two or three weeks each year

for maintenance (L.F. 167). Further, there have been occasions when mechanical or other difficulties have precluded Dyno from manufacturing its products (L.F. 167). In December 1989, a mechanical failure forced Dyno to suspend operations for 24 days (L.F. 167). Another mechanical failure forced the shut-down of Dyno's manufacturing operations for 39 days during December 1992 and January 1993 (L.F. 167). During the Great Flood of 1993, Dyno's manufacturing facilities were shut down for at least three weeks due to the flood's impact on transportation (L.F. 167). During all of these periods, Dyno continued to pay forty-five percent of the fixed operating costs of the Utilities Plant (L.F. 167), even though Dyno was not operating its part of the Facility.

Part III, section VIII of the Utility Agreement requires Dyno to reimburse Hercules for the variable costs of producing electricity, including fuel costs, the net cost of purchasing supplemental electricity from Union Electric or Ameren as explained below, and other variable costs such as sales and use tax on taxable purchases for the Utilities Plant (L.F. 64-65, 88-89, 93-94, 100-01). The variable costs are apportioned between Hercules and Dyno based upon their respective consumption of the electricity at the Facility (L.F. 64-65, 88-89, 93-94, 100-01).

Although Dyno's payments to Hercules pursuant to the Utility Agreement are based upon cost reimbursement, the Utility Agreement does use terms like "purchase," "sale," and "title" in several places (L.F. 160-63).

Invoicing and Reimbursement

Dyno reimburses Hercules monthly for Dyno's share of the fixed and variable operation costs of the Utility Plant (L.F. 168). Hercules invoices Dyno on a monthly basis therefor (L.F. 168). Those invoices designate the charge as follows: "FOR CHARGES INCURRED BY THE MCW PLANT ON YOUR BEHALF FOR THE MONTH OF …" (L.F. 168). The invoice lists "power charges"

consisting of an "OPERATING COST" and "ENERGY COST" (L.F. 168). The "operating cost" is for the fixed costs and the "energy cost" is for the variable costs (L.F. 168).

Dyno has always requested, and Hercules has always provided, backup documentation to support all of the costs reflected on the invoices (L.F. 168). Hercules also makes its actual invoices available to Dyno for its review and verification of costs (L.F. 168). Dyno has audited Hercules regarding its costs in this regard (L.F. 168).

During the periods October 1994 through September 1997 ("Tax Periods"), 53.6 percent of Dyno's reimbursements to Hercules pursuant to the Utility Agreement were for fixed costs and 46.4 percent of Dyno's reimbursements for variable costs (L.F. 168).

Treatment of the Electric Utility Payments

Dyno and Hercules have always considered and treated their business relationship regarding the cost of the Utilities Plant as an agreement to share the costs of producing utilities for the Facility they shared (L.F. 91, 95, 102). Consequently, Hercules never charged Dyno sales or use tax on the cost reimbursements under the Utility Agreement, and Dyno never provided Hercules with an exemption certificate or other evidence of exemption (L.F. 168).

After auditing Dyno for more than two weeks at the Facility, the Director's auditor and his supervisors concluded that Dyno and Hercules shared the costs of producing utilities at the Utilities Plant

serving the Facility they shared, and concluded that Dyno was due a refund of the tax it remitted on the cost reimbursements (Dep. 11, 16-17, 22-23, 45).[3]

In 1991, Ameren investigated the Utilities Plant to determine whether its production of electricity was consistent with Ameren's tariffs. Based upon its investigation, Ameren determined that Hercules was not a utility violating Ameren's tariffs, because it was merely sharing costs with Dyno rather than selling electricity to Dyno (L.F. 88-89, 96, 102).

Neither Dyno nor Hercules has a certificate of authority from the Missouri Public Service Commission ("PSC") to sell electric power at retail in Missouri (L.F. 168).

Returns and Refund Claim

Dyno has filed, and continues to file, Missouri sales and use tax returns on a monthly basis (L.F. 96-97). For each of the Tax Periods, Dyno remitted use tax and statewide local use tax, if applicable, on the cost reimbursements to Hercules (L.F. 96-97). The total amount of use tax and statewide local use tax remitted on the cost reimbursements for during the Tax Periods was $85,225.64 (L.F. 96-97).

On November 20, 1997, Dyno filed a refund claim with the Director for its use tax and statewide local use tax remitted on the cost reimbursements (L.F. 169).[4] The refund claim stated as the

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[3] Citations to (Dep.) are to the Deposition of the Director's auditor, Richard Diein, taken in this matter.

[4] The original refund claim filed with the Director was for $86,703.19. On April 10, 1998, the Director received amended returns from Dyno with a cover letter stating that the correct refund amount was $85,225.64 (L.F. 169).

"reason for overpayment": "Taxes were incorrectly accrued on purchases that were not taxable to Dyno Nobel, Inc." (L.F. 169). The Director's auditor stated that the refund claim was sufficiently broad to include all of the theories for the refund presented to the Commission, including the theory that any tax due would be sales tax from Hercules and not use tax from Dyno (Dep. 32-33).

On November 12, 1999, the Director issued a final decision denying the claim for refund (L.F. 170). As the basis for the denial, the Director stated, "Correct amount of tax was paid by Dyno Nobel Inc." (L.F. 170).

Commission's Decision

Upon the parties' cross-motions for summary determination, the Commission entered its Memorandum and Order on March 28, 2001 (L.F. 156-175). In the Commission's conclusions of law, the Commission agreed with the conclusion of the Director's auditor and his supervisors that Dyno's claim for refund included all of the theories presented to the Commission supporting Dyno's claim for refund (L.F. 170-172).

The Commission concluded that Dyno's cost reimbursements to Hercules pursuant to the Utility Agreement constituted the taxable purchase of electricity by Dyno (L.F. 172-173). The Commission also concluded that, notwithstanding Dyno's request for a refund of use tax and related statewide local use tax, the tax before the Commission was a sales tax (L.F. 175). The Commission stated that Sections 144.020.1, 144.021 and 144.080.1 impose the sales tax upon sellers, and imposes upon the seller the burden to remit the tax to the Director (L.F. 175). Nonetheless, because purchasers bear the economic burden of the sales tax, the Commission concluded that Dyno was not entitled to a refund of the taxes paid (L.F. 175).

STATEMENT OF THE ISSUES

Dyno and Hercules share a manufacturing facility designed for one operator with one electric loop circuit running through it, and one Utilities Plant designed to provide the steam, electricity and water necessary for the Facility. When Dyno purchased part of the Facility in 1985, Dyno and Hercules arranged to share utilities by agreeing to split the costs of operating the Utilities Plant. Specifically, Dyno and Hercules agreed to split the fixed costs on a basis whereby Dyno reimburses Hercules for forty-five percent of the Utilities Plant's fixed costs, and reimburses Hercules for the variable costs based upon each parties' respective power consumption. Thus, Dyno reimburses Hercules for the cost of operating the Utilities Plant even when Dyno consumes no electricity. Dyno, Hercules, Ameren (the utility holding the tariff for the geographical area in which the Facility and Utilities Plant are located), and the Director's own auditor and his supervisors, agreed that the economic substance of this relationship between Dyno and Hercules is a cost reimbursement rather than the sale of electricity. However, the Utility Agreement uses the terms "purchase," "sale," and "title" in several places. Missouri law provides that the economic realities of transactions, rather than labels, determine the taxability of the transactions. Are Dyno's reimbursements of costs to operate the Utilities Plant that serves the Facility subject to Missouri use tax as purchases of electricity?

Missouri law expressly excludes from the use tax transactions that are subject to Missouri's sales tax. Missouri sales tax law applies to sales from a Missouri vendor to a Missouri consumer. Missouri sales tax law imposes the sales tax upon vendors, unless a purchaser has submitted to a vendor a written claim of exemption. There is no dispute that the Facility and the Utilities Plant are located entirely in Missouri. Dyno never provided Hercules any written claim of exemption. Is Dyno subject to Missouri sales or use tax on those reimbursements, even if the reimbursements are deemed to be purchases of electricity?

STANDARD OF REVIEW

The decision of the Commission shall be upheld if it is: (1) authorized by law; (2) supported by competent and substantial evidence upon the whole record; (3) if no mandatory procedural safeguards are violated; and (4) where the Commission has discretion, it exercises discretion in a way that is not clearly contrary to the Legislature's reasonable expectations. Section 621.193; *Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186 (Mo. banc 1996). Furthermore, because this Court is reviewing the issuance of a summary determination against Dyno, it reviews the record in a light most favorable to Dyno. *Tauchert v. Boatmen's National Bank of St. Louis*, 849 S.W.2d 573 (Mo. banc 1993).

This case involves the construction of Sections 144.020.1(3), 144.010.1(9) and 144.060, all of which are tax imposition statutes. Tax imposition statutes are strictly construed against the Director, and if the right to tax is not plainly conferred by statute, it will not be extended by implication. *United Air Lines, Inc. v. State Tax Commission*, 377 S.W.2d 444, 448 (Mo. banc 1964), *quoting Leavell v. Blades*, 141 S.W. 893, 894 (Mo. 1911) ("When the tax gatherer puts his finger on the citizen, he must also put his finger on the law permitting it.").

Finally, this Court's interpretation of Missouri's revenue laws is *de novo*. *Zip Mail Services, Inc. v. Director of Revenue*, 16 S.W.3d 588, 590 (Mo. banc 2000).

POINTS RELIED UPON

I.

THE ADMINISTRATIVE HEARING COMMISSION ERRED IN DENYING APPELLANT'S MOTION FOR SUMMARY DETERMINATION AND GRANTING THE DIRECTOR'S MOTION FOR SUMMARY DETERMINATION BECAUSE, UNDER SECTIONS 621.189 AND 621.193, THAT DECISION IS NOT AUTHORIZED BY LAW OR SUPPORTED BY COMPETENT AND SUBSTANTIAL EVIDENCE IN THAT APPELLANT'S REIMBURSEMENTS TO HERCULES FOR THE COSTS OF OPERATING THE ON-SITE UTILITIES PLANT ARE NOT SUBJECT TO MISSOURI TAX UNDER SECTIONS 144.020.1(3) AND 144.010.1(9) BECAUSE THE COST REIMBURSEMENTS DO NOT CONSTITUTE THE PURCHASES OF ELECTRICITY WITHIN THE MEANING OF THOSE SECTIONS.

McDonnell Douglas Corporation v. Director of Revenue, 945 S.W.2d 437 (Mo. banc. 1997);

Scotchman's Coin Shop, Inc. v. Administrative Hearing Commission, 654 S.W.2d 873 (Mo. banc 1993);

Massman Construction Company v. Director of Revenue, 765 S.W.2d 592 (Mo. banc 1989);

Rosehill Gardens, Inc. v. Director of Revenue, Case Number 95-2875RV (Mo. Admin. Hrg. Comm'n 1997);

Section 144.010.1(5);

Section 144.010.1(9);

Section 144.020.1(3);

Section 621.189; and

Section 621.193.

II.

THE ADMINISTRATIVE HEARING COMMISSION ERRED IN DENYING APPELLANT'S MOTION FOR SUMMARY DETERMINATION AND GRANTING THE DIRECTOR'S MOTION FOR SUMMARY DETERMINATION BECAUSE, UNDER SECTIONS 621.189 AND 621.193, THAT DECISION IS NOT AUTHORIZED BY LAW OR SUPPORTED BY COMPETENT AND SUBSTANTIAL EVIDENCE IN THAT, ASSUMING, *ARGUENDO*, THAT APPELLANT'S REIMBURSEMENTS TO HERCULES FOR THE COSTS OF OPERATING THE UTILITIES PLANT ARE SUBJECT TO MISSOURI TAX, APPELLANT WAS NOT LIABLE FOR USE TAX ON THOSE REIMBURSEMENTS BECAUSE THE APPLICABLE TAX WOULD BE MISSOURI SALES TAX IMPOSED ON THE VENDOR, NOT UPON APPELLANT.

House of Lloyd v. Director of Revenue, 884 S.W.2d 271 (Mo. banc 1994);

Olin Corporation v. Director of Revenue, 945 S.W.2d 442 (Mo. banc 1997);

Concord Publishing House, Inc. v. Director of Revenue, 916 S.W.2d 186 (Mo. banc 1996);

Bratton Corporation v. Director of Revenue, 783 S.W.2d 891 (Mo. banc 1990);

Section 144.020.1(3);

Section 144.190;

Section 144.210;

Section 144.610;

Section 144.615(2);

Section 144.696;

Section 621.189; and

Section 621.193.

ARGUMENT

I.

THE ADMINISTRATIVE HEARING COMMISSION ERRED IN DENYING APPELLANT'S MOTION FOR SUMMARY DETERMINATION AND GRANTING THE DIRECTOR'S MOTION FOR SUMMARY DETERMINATION BECAUSE, UNDER SECTIONS 621.189 AND 621.193, THAT DECISION IS NOT AUTHORIZED BY LAW OR SUPPORTED BY COMPETENT AND SUBSTANTIAL EVIDENCE IN THAT APPELLANT'S REIMBURSEMENTS TO HERCULES FOR THE COSTS OF OPERATING THE ON-SITE UTILITIES PLANT ARE NOT SUBJECT TO MISSOURI TAX UNDER SECTIONS 144.020.1(3) AND 144.010.1(9) BECAUSE THE COST REIMBURSEMENTS DO NOT CONSTITUTE THE PURCHASES OF ELECTRICITY WITHIN THE MEANING OF THOSE SECTIONS.

Introduction

This appeal addresses the extremely unique business relationship between Dyno and Hercules. The Facility shared by Dyno and Hercules was originally owned entirely by Hercules. As a result of its design for one operator, the Facility has one electric loop circuit running throughout the Facility and has one Utilities Plant designed to provide steam, electricity and water necessary for the Facility.

When Dyno purchased a portion of the Facility in 1985, Dyno and Hercules were required to make arrangements to share utilities due to the Facility's design. The parties agreed to allocate the costs of the Utilities Plant such that Dyno paid forty-five percent of the Utilities Plant's fixed costs and paid its share of the variable costs based upon its share of the consumption of electricity.

Dyno remitted use tax upon its reimbursements to Hercules for both the fixed and variable electric energy costs of the Utilities Plant, and subsequently sought a refund of these amounts. The Commission concluded that Dyno's cost reimbursements to Hercules constituted the taxable purchase of electricity. The Commission's conclusion in this regard is not authorized by Missouri law. Dyno's reimbursements to Hercules for the cost of the Utilities Plant shared by the parties do not constitute purchases of electricity within the meaning of Sections 144.020.1(3) and 144.010.1(9) because the reimbursements are not in consideration for any transfer of electricity.

A. The Cost Reimbursements are Not Purchases of Electricity Subject to Tax.

Section 144.020.1(3) imposes Missouri sales tax upon "the basic rate paid or charged on all sales of electricity or electrical current." A "sale" is a transfer of title for consideration. Section 144.010.1(9); *McDonnell Douglas Corporation v. Director of Revenue*, 945 S.W.2d 437 (Mo. banc 1997). Dyno's cost reimbursements are not subject to Missouri tax because the payments are reimbursements under a cost-sharing agreement and not for the transfer of electricity.

Dyno's payments to Hercules under the cost-sharing agreement have both a fixed and variable component. Dyno was liable for the fixed component of the costs of the Utilities Plant, ***regardless of whether it consumed electricity*** (L.F. 94, 100-01). The fixed component of the reimbursements, comprising 53.4 percent of Dyno's payments to Hercules during the Tax Periods, obviously was not "consideration" for the transfer of title of electricity or electric current since it was due even when Dyno consumed no electricity. Indeed, the understanding of all parties, Dyno, Hercules, Ameren, and even the Director's accountants, was that the economic substance of the transactions shows that they were not purchases of electricity. Furthermore, all of the documentary evidence, other than some terms used in the Utilities Agreement, support that understanding.

The invoices Hercules sends to Dyno reflect that payment is sought for charges incurred at the Utilities Plant (L.F. 168). The invoices relate not only to utilities, but also to other shared operations including the common Facility storeroom and the crossing signal (L.F. 168). Each invoice includes detailed accounting records that Dyno can, and has, audited to ensure proper allocation of the costs (L.F. 168). Further evidencing the collaborative nature of the relationship between Dyno and Hercules is the fact that Dyno is partly responsible for the production of the electricity in that Dyno heats the water that enters the boilers to produce the steam that drives the turbines and generators (L.F. 160). This behavior is completely inconsistent with the Commission's characterization of the cost reimbursements as the taxable sale of electricity between a vendor and a purchaser.

Instead, the relationship between Dyno and Hercules is analogous to college roommates sharing the costs of a telephone in a shared apartment. For instance, three college students might live in one apartment having one telephone line installed in the name of one of the students. That student is responsible for paying the bill, but has made arrangements for reimbursement of the costs by the other two students. After paying the bill, that roommate takes the bill and divides the local charge and tax thereon by three. To that amount, he adds the cost of each of his roommates' long distance calls plus tax thereon and is reimbursed this amount by each roommate. Likewise, when the students crave a pizza, they order one by phone, one student picks up and pays for the pizza, and is reimbursed by the other students. The students are not selling pizza to each other; they are sharing the cost of purchasing the pizza. Under the Commission's analysis, the cost reimbursements are taxable sales.

This result was clearly not intended by the Legislature, as demonstrated by its definition of "person" in Section 144.010.1(5) to include "any other group or combination acting as a unit." Simply put, a "group or combination acting as a unit" for a transaction is a single "person." The group, like the

college roommates and Dyno and Hercules, cannot "sell" to itself, and is therefore not subject to sales tax on these types of transactions. Therefore, the Commission's decision to the contrary should be reversed by this Court.

B. Interested Parties Have Concluded That Dyno's Cost Reimbursements are Not Purchases of Electricity.

After evaluating the admittedly unique relationship between Dyno and Hercules, interested third parties have concluded that Hercules is not selling electricity to Dyno. Hercules is not a PSC certificated provider authorized to sell electricity at retail. Ameren has the PSC's authority for the territory serving the Facility. It would undoubtedly serve Ameren's interest to treat the cost reimbursements as the sale of electricity, and a violation of its tariffs, thus triggering a requirement for Dyno to purchase electricity from Ameren. However, upon its investigation in 1991, Ameren determined that Dyno's cost reimbursements to Hercules did not constitute a retail sale of electricity (L.F. 88-89, 96, 102).

Indeed, the Director's own auditor and audit supervisors admitted that, in the absence of language in the Utility Agreement, the transaction between Dyno and Hercules would be treated as a nontaxable cost-sharing agreement rather than the sale of electricity (Dep. 17, 45-46). Therefore, it is clear that the examination of the relationship by interested, adverse parties demonstrates that Dyno's cost reimbursements are not taxable sales of electricity.

C. The Commission's Emphasis on Words Over Substance is Inconsistent with Missouri Law.

The Commission emphasized particular language in the Utility Agreement to support its conclusion that Dyno's cost reimbursements constitute taxable purchases of electricity. Indeed, the

Commission considered the contract language critical in rejecting the Director's auditor's and his supervisors' acceptance of Dyno's position that the transactions between Dyno and Hercules did not constitute the taxable sale of electricity ("[T]he auditor did not have a copy of the Utilities Contract before him" (L.F. 170), and "the auditor did not have a copy of the contract before him, and he was not reviewing the refund claim" (L.F. 173)). If one were to take the Commission's position at face value, Dyno's cost reimbursements to Hercules would be excluded from tax if the Utility Agreement were rewritten to clearly reflect that the reimbursements are a cost sharing. Furthermore, in emphasizing particular language of the Utility Agreement, the Commission largely ignored language in the Asset Purchase Agreement, the agreement that precipitated the Utility Agreement. According to the Asset Purchase Agreement, the Utility Agreement was to further "the provision of common services . . . including . . . materials and utilities" (L.F. 160).

The Commission's emphasis of form over substance stands established tax precedent on its head. It is undisputed that Missouri sales and use taxation is determined by the economic substance of the transaction, and not by the parties' characterizations thereof. *See, e.g., Scotchman's Coin Shop, Inc. v. Administrative Hearing Commission*, 654 S.W.2d 873, 875 (Mo. banc 1983); *Massman Construction Company v. Director of Revenue*, 765 S.W.2d 592, 594 (Mo. banc 1989). Moreover, the Commission's own decisions prior to this case are consistent with this Court's holdings in this regard. *See Rosehill Gardens, Inc. v. Director of Revenue*, Case Number 95-2875RV (Mo. Admin. Hrg. Comm'n 1997) ("The Director argues that based on the manner in which Rosehill structured its transactions, it made taxable retail sales of tangible personal property. ***The fact***

that Rosehill invoiced and collected sales tax as a retailer is irrelevant.[5] We cannot exalt form over substance in sales tax matters. Taxation is not based on how a taxpayer structures a transaction; it is based on the economic realities of the transaction.").

The Director's auditor recognized this principle. The Director's auditors are instructed to determine taxability based upon the substance of transactions and not by exalting form over substance (Dep. 39-40). In this case, the Director's auditor concluded that the reimbursements were not taxable because Hercules' invoices were for charges incurred on Dyno's behalf (Dep. 20-21), and Dyno was required to reimburse Hercules for the costs of the Utilities Plant ***whether or not Dyno received any electricity*** (Dep. 41-42). The auditor conceded that, even if the Utility Agreement expressly characterized the transactions as a cost sharing, he would still view the economic reality of the transaction to determine taxability (Dep. 39-40).[6]

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[5] Emphasis added here and throughout, unless otherwise noted.

[6] The Commission, realizing that excessive emphasis on contract words was inconsistent with state law, stated that its decision was based on the economic reality that "the electricity is produced on Hercules' property by Hercules' generators operated by Hercules' employees, and that Hercules holds 'title' to the electricity until it transmits the electricity to Dyno at a certain physical point" (L.F. 173). This is contrary to the Commission's finding of fact that "Hercules draws water from the Mississippi River, treats it, ***and pumps it to Dyno's part of the facility. Dyno heats the water and pumps it back to Hercules*** for use in boilers that produce steam … used … to drive steam turbines and generators that produce electricity that Hercules and Dyno use" (L.F. 160).

The Commission's decision would reverse the long-standing Missouri rule that the economic realities, and not the form of the transaction, determine Missouri taxability. Because the Commission's decision would reverse this long-standing rule, this Court should reverse the Commission and determine that Dyno is entitled to a refund of Missouri use tax paid because its cost reimbursements to Hercules do not constitute the taxable purchase of electricity.

II.

THE ADMINISTRATIVE HEARING COMMISSION ERRED IN DENYING APPELLANT'S MOTION FOR SUMMARY DETERMINATION AND GRANTING THE DIRECTOR'S MOTION FOR SUMMARY DETERMINATION BECAUSE, UNDER SECTIONS 621.189 AND 621.193, THAT DECISION IS NOT AUTHORIZED BY LAW OR SUPPORTED BY COMPETENT AND SUBSTANTIAL EVIDENCE IN THAT, ASSUMING, *ARGUENDO*,THAT APPELLANT'S REIMBURSEMENTS TO HERCULES FOR THE COSTS OF OPERATING THE UTILITIES PLANT ARE SUBJECT TO MISSOURI TAX, APPELLANT WAS NOT LIABLE FOR USE TAX ON THOSE REIMBURSEMENTS BECAUSE THE APPLICABLE TAX WOULD BE MISSOURI SALES TAX IMPOSED ON THE VENDOR, NOT UPON APPELLANT.

The Commission's decision denying Dyno's refund claim is based upon its conclusion that Hercules sold electricity to Dyno. However, assuming, *arguendo*,that the cost reimbursements constituted purchases of electricity, Dyno is still not liable for use tax on these payments because:

(1) taxable in-state transfers are exempt from Missouri use tax under Section 144.615(2) because they are subject to Missouri sales tax; and

(2) any liability for Missouri sales tax would be upon Hercules and not Dyno because Dyno submitted to Hercules no written evidence of exemption.

Missouri's sales and use tax schemes are complementary and are "designed to assure that purchases of tangible personal property for valuable consideration by a Missouri purchaser receive identical treatment no matter what the geographic location of the seller." *House of Lloyd, Inc. v.*

Director of Revenue, 884 S.W.2d 271, 273 (Mo. banc 1994). Sales tax is imposed on retail sales that take place in Missouri. By contrast, the use tax is designed to tax out-of-state purchases of tangible personal property by purchasers who use, consume or store the property in Missouri. *Olin Corporation v. Director of Revenue*, 945 S.W.2d 442 (Mo. banc 1997).

The tax statutes themselves provide this result. Section 144.610 imposes the use tax upon the storage, use or consumption of tangible personal property. On its face, it imposes tax on all purchases that are used, consumed or stored in Missouri. Section 144.615(2) exempts from the use tax, "property, the gross receipts from the sale of which are required to be included in the measure of the tax imposed under the Missouri sales tax law[.]"

There is no dispute that Hercules does business in Missouri nor is there any dispute that the transactions occurred entirely at the Facility located in Missouri. Thus, the cost reimbursements, if taxable at all, are subject to Missouri sales tax under Section 144.020.1(3). The Commission did not dispute that unassailable conclusion, but it held that Dyno was liable for sales tax because in "economic substance" the purchaser bears the burden of the sales tax (L.F. 175). This conclusion is incorrect. Section 144.210 provides that the Director may collect sales tax from a purchaser ***only*** if the purchaser provided an exemption certificate to the vendor. *See, e.g., Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186, 189 (Mo. banc 1996); *Bratton Corporation v. Director of Revenue*, 783 S.W.2d 891, 893 (Mo. banc 1990). Dyno never provided Hercules with an exemption certificate or other written evidence of exemption for the cost reimbursements (L.F. 168). Therefore, the Commission's retention of Dyno's Missouri use tax payments to satisfy this alleged liability of another taxpayer is contrary to Missouri law.

Dyno paid $85,225.64 in Missouri use tax during the Tax Periods based upon its cost reimbursement payments to Hercules. This tax was overpaid because the cost reimbursements (even if they constitute the taxable purchase of electricity) are expressly exempt from Missouri use tax under Section 144.615(2). Because Dyno overpaid the tax, Dyno is entitled to a refund pursuant to Sections 144.696 and 144.190.

CONCLUSION

Based on the foregoing, Appellant respectfully request that this Court reverse the Commission and remand with instructions to sustain Appellant's refund claim.

Respectfully Submitted,

BRYAN CAVE LLP

Edward F. Downey, #28826
221 Bolivar Street, Suite 101
Jefferson City, Missouri 65101
Telephone: (573) 556-6622
Facsimile: (573) 556-6620

Juan D. Keller, #19864
B. Derek Rose, #44447
One Metropolitan Square
211 North Broadway, Suite 3600
St. Louis, Missouri 63102
Telephone: (314) 259-2000
Facsimile: (314) 259-2020

Attorneys for Appellants

CERTIFICATE OF SERVICE

I hereby certify that two true and accurate copies of the foregoing, as well as a labeled disk containing the same, were mailed first class, postage prepaid or hand-delivered this _____ day of November 2001, to Deputy State Solicitor Alana Barragan-Scott, P.O. Box 899, Jefferson City, Missouri 65102.

_____

CERTIFICATE REQUIRED BY SPECIAL RULE 1(C)

I hereby certify that the foregoing brief includes the information required by Supreme Court Rule 55.03 and complies with the limitations contained in Supreme Court Special Rule 1(b). The foregoing brief contains 5,897 words.

The undersigned further certifies that the disk simultaneously filed with the briefs filed with this Court under Supreme Court Rule 84.05(a) has been scanned for viruses and is virus-free.

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